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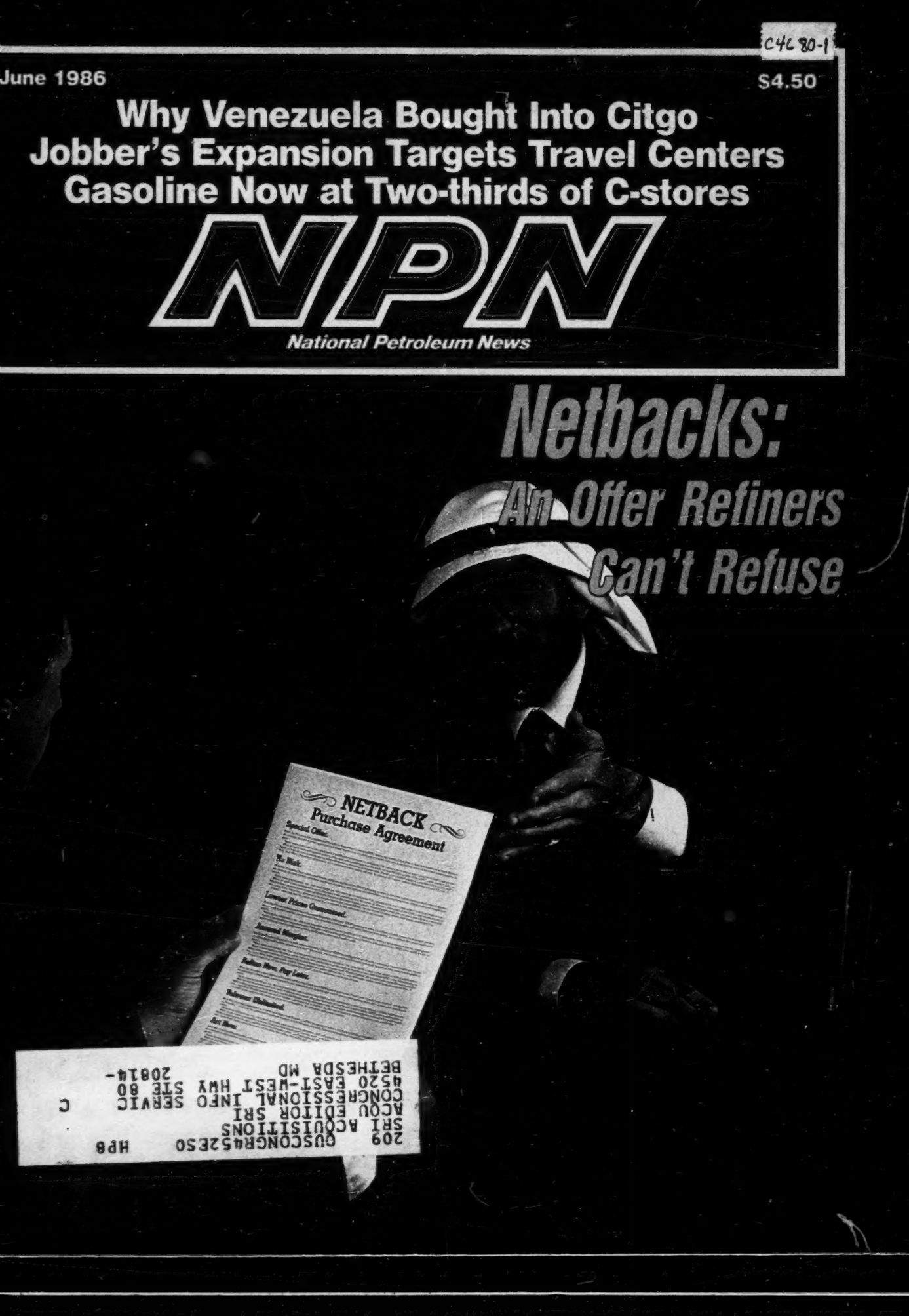
Why Venezuela Bought Into Citgo
Jobber's Expansion Targets Travel Centers
Gasoline Now at Two-thirds of C-stores

NPN

National Petroleum News

Netbacks: An Offer Refiners Can't Refuse



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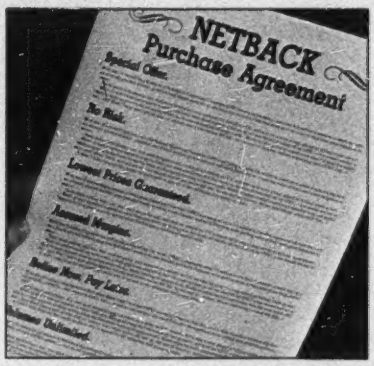

Netback pricing deals have quickly caught on in the oil industry as a means of locking in markets for producers and margins for refiners. Our in-depth report looks at how netbacks work and their affect on retail prices. **Page 34**

Venezuela has launched an aggressive campaign to not only preserve, but expand its share of the American oil market by selling directly to consumers through joint ownership deals. **Page 38**

Atlanta jobber Herb Ingersoll is moving in the opposite direction of many jobbers. While others consolidate, he's expanding with plans for a network of travel centers in the Southeast. **Page 44**

• TRENDS

Retail Price Wars: Playing An Old Game Under New Rules

When retail gasoline postings were slow to follow the sharp downturn in world crude oil prices earlier this year, some "experts" said that refiners and marketers were in such dire need of better profit margins that they wouldn't get involved in deep retail price-cutting or price wars this time.

Some independents who are nothing less than artists in playing the price-cutting game giggled over the reasoning of the "experts." At the same time, however, these indies say there are changing conditions which are bringing about new trends in retail pricing.

A combination of the oil companies removing certain credit incentives, high gasoline prices (as compared to the pre-1980's), and the virtual disappearance of "restoration moves" once practiced by the majors now restrains price-cutting to some degree, says one former cut-rater.

There was a time, this marketer points out, when all of the economics encouraged people like him to play the price-cutting game. This was back before the 1970s.

To begin with, he says, in those days a private-brand independent could often find refiner-suppliers willing to give him from 30 to 45 days to pay for gasoline he bought from them. If the marketer could speed such product through his pumps, he had it sold before he had to pay for it. While many at the time had never heard of such sophisticated terms as "cash flow," they did know that such an arrangement, whereby they could operate on somebody else's money, was a splendid one, indeed.

One way to quickly move the gasoline on through the pumps was to cut prices, this person adds, and the general level of retail prices for all products at the time enabled one to do this in a way to catch the customer's eye. With gasoline retailing at around 30¢ gal., a 2¢ or about a 7% reduction represented a real bargain. The 40¢ savings on a 20 gal. purchase might buy a jug of milk at prices back then.

A 2¢ gal. price cut when gasoline is a buck a gallon doesn't have the same impact on the customer, says this marketer, because the 40¢ savings won't buy nearly as much of something else. And the market, he adds, "won't let you have much more than that even if you could afford a larger reduction."

But the big thing that causes some to be more cautious and a little slower in cutting prices involves the lack of those "restoration moves" of the past.

It used to be, this indie says, that price wars and market restorations followed certain patterns and cycles. Some price-cutters, usually private-branders, would begin whittling away at prices until others followed and a market reached bottom. Then, usually, some major oil company would initiate an effort to restore prices to their normal level. Typically, unless some marketer really had a mad on, all would follow such a move for a day or two and then the downward trend cycle would begin again.

"You could usually count on these up and down cycles several times a year," says this indie. "Over a year's time, you would average out on pretty good margins, although you might be on bottom part of the time."

This situation has changed, too, he says. "Now, you see prices drifting down to near the cost of product and they stay down."

The changed conditions haven't stopped the price wars or price-cutting. Indeed, while it generally took them longer to do so, retail prices in many markets had pretty well caught up with the tumbling crude oil postings by early-May. Most majors, who earlier had moved down on their dealer tankwagon prices rather slowly, had for the most part dropped them to levels competitive with jobber wholesale rack prices. Branded dealer retail postings in some of the hot markets were reflecting this.

If the current pattern that this independent speaks of is followed, the retail prices may stay down for awhile.

The downward movement of retail prices this spring, while somewhat slow in developing, apparently proves that the industry will always have price-cutting when supply is plentiful. Although certain incentives to cut them have been removed or have changed, some marketers still see the need to shade their postings for such reasons as trying to gain more gallonage.

—Marvin Reid

• MARKETPLACE AT A GLANCE

AVERAGE GASOLINE PRICES IN THE U.S. (per gal.)

MARCH	Gasoline (All types)	Leaded Regular	Unleaded Regular	Unleaded Premium
U.S. City Avg.	$ .983	$ .894	$ .981	$1.160
Regions:				
Northeast	1.058	.974	1.039	1.195
North Central	.919	.852	.927	1.107
South	.973	.886	.971	1.139
West	1.008	.902	1.010	1.194

Source: U.S. Dept. of Labor, Bureau of Labor Statistics.

STOCKS (Add 000 bbl.)

	5/2/86	5/3/85
Gasoline (total)	206,261	213,920
Gasoline (Unleaded)*	108,652	102,002
Jet Kerosine	39,220	34,996
Distillates	96,059	97,286
Residual	36,301	45,527

**Included in gasoline total.*
Source: American Petroleum Institute.

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NATIONAL PETROLEUM NEWS JUNE 1986

Unstable Prices, Company Cutbacks Cloud Big Driving Season Forecast

Now that Memorial Day has ushered in the traditional summer driving season, gasoline marketers are looking at what probably will be the best demand period they've had in recent years.

It's not very likely the volumes will be high enough to compromise the peak year performances of 1978 and 1979. But with a few breaks here and there, they can be expected to be bubbling along at levels that will make everybody happy. Better than last year, a turn-around year, but not record-breaking. Seven out of 10 gal. will be unleaded.

All of the ingredients are out there now for fast action in the marketplaces. With all three grades selling below $1 gal., the low retails are luring many motorists back on the road. So are the cancelled vacation plans of many who otherwise would have gone overseas but have been frightened off by the terrorism abroad. The devalued American dollar is also an incentive to stay home this year.

American Automobile Assn. says it is anticipating at least a 5% increase in driving this summer. This, on top of the 6% that was registered last year.

But there are some worrisome factors out there, too.

- The industry is contracting and sweating out the collapse of the crude oil market. Two-thirds of the top 20 companies had minus signs on their first-quarter earnings reports. Three had losses, not as a result of bad marketing but as a result of restructuring and re-evaluation of inventories and assets.
- Capital spending programs are being cut drastically—by the hundreds of millions of dollars. Gross revenues were down 25% to 35% almost everywhere, weakening cash flows and operating funds.
- Many companies are trimming personnel rosters. Exxon sent shock waves through the industry by inviting 40,000 of its employees—about one-fourth of its global total—to take early retirement or resignation bonuses. Subsequently, Exxon said it was really only shooting for a 6,000-man reduction, but even that was an awesome figure. Amoco said it was cutting the work force of its production subsidiary by 15% or 1,500 people. Pennzoil said it was lopping off 600 people, or about 8% of its personnel. Marathon said it dropped 1,000 production personnel in the first quarter of this year. Chevron, Occidental and others also have announced prunings and early retirement programs.
- Wholesale and retail prices will probably be shaky all summer. They relate entirely to the continuing fall of international and domestic crude oil postings. Just about everything hinges on Saudi Arabia which still shows no true signs of relenting and reducing the flood of crude that it has been putting on the market. In April, crude abroad and at home was worth about $11 to $12 bbl., but there was still talk floating around that the bottom may go as low as $5 to $7 bbl., which would exert incredible pressures on oil companies and economies alike.
- The weaknesses of the crude oil markets and retail operations are having radiant effects throughout the economy. Banks with heavy loan schedules to producers and suppliers are worrying as cash flows dwindle and paybacks get hung up. Some states with oil economies, like Texas and Oklahoma, are already having boomerang effects. Jobbers, distributors and retailers are feeling cash flow pressures, too, and some are being squeezed dry.

There are a lot of goodies out there, too, however.

The first-quarter earnings reports, for example, showed that downstream operations turned in strong profits in January, February and March despite the plummeting wholesale/retail price structures.

Exxon, for example, made $160 million in domestic downstream profits in the first quarter which, when compared to last year's $13 million, reflected an increase of 1,131%. Phillips topped them all, with earnings of $98 million this year versus $2 million in 1985 for an increase of 4,800%. Amoco, which registered a 30% decrease in its first-quarter earnings had an 850% increase in worldwide downstream profits. Mobil had refining-marketing-transportation profits of $51 million in the U.S. this year versus a loss of $11 million in first-quarter 1985. Texaco earned $301 million worldwide in marketing compared with a loss of $27 million last year.

In the corporate picture, Exxon continued to dominate everything despite its displacement by *Fortune* magazine as the No. 1 corporate entity in the country (*Fortune* gave the nod to General Motors on the basis of 1985 revenues alone). Exxon netted $1.7 billion in the first quarter, up

(Continued on following page.)

Halbouty: A Lone Voice or Rising Tide?

Michel T. Halbouty, an outspoken independent Texas oil producer, thinks there's something wrong with oil executives' when they make sharp personnel and exploration cutbacks as a quick fix for current income problems.

"Where is the morality in business when CEOs don't give a damn for the human element any more?" he asked. Halbouty has been in the oil industry a long time and is now in his seventies, he said he didn't understand "the change in the morality of U.S. business."

More reasonable and humane, he said, would be to cut dividends instead. He calculated Chevron, Exxon and Mobil, to name just three, could make $6,520 million available "to maintain personnel and do some exploration" simply by cutting back, not eliminating, dividends. Chevron has 343 million shares of stock, Exxon 731 million, Mobil 408 million; total 1,482 million shares. Chevron pays $2.40 annual dividend, Exxon $3.60, Mobil $2.20. If they cut back by $1.40, $2, and $1, respectively, it would total $4.40, or $6,520 million on 1,482 million shares.

He said this would keep people working, maintain exploration, find new reserves, increase company assets, decrease imported oil, and enable companies to pay more dividends later.

Halbouty, the CEO of Michel T. Halbouty Energy Co., Houston, blamed the layoffs and cutbacks on "immoral" corporate raids which forced some oil companies to go heavily into debt. He added that the recent drop in oil prices "only accentuated it." NPN

Driving Season Forecast, Continued

29% over 1985. Peer companies Mobil, Texaco and Chevron all had profit increases in the first quarter. From there on down and with the exception of Sun and Ashland, all the others had decreases vis a vis 1985. Marathon Petroleum, which has been making money for U.S. Steel Corp. since it was acquired three years ago, said it had a first-quarter operating loss of $133 million compared to a profit of $293 million last year.

Most of the companies pretty well agreed that if retail price levels continue in the 60¢ and 70¢ range for the duration of the second quarter, the first-half revenues and nets would be depressed everywhere.

On the volume side, American Petroleum Institute noted in April that gasoline demand had increased 6% in March alone and that the first quarter was 3.2% ahead of last year. Another promising factor was that demand in April was already in the 7 million b/d-plus range which is roughly a month ahead of where it has been in recent years.

Prices aren't expected to improve during the summer months barring a bottoming out and improvement in crude oil acquisition costs. There was some firming up of retails in May, immediately prior to the Memorial Day weekend. But how long they'll prevail is conjectural. All in all, however, few complaints have been heard about margins and in the absence of such carping and criticism it has to be assumed that most margins are relatively respectable.

An interesting look at what's ahead was offered by Conoco's president, Constantine S. Nicandros.

Nicandros, addressing an API meeting in Houston in mid-April, said about the only thing truly predictable at this time is that the future will be characterized by tight supplies and sharp price swings. He outlined three scenarios ranging from $5 bbl. crude up to $35 bbl. crude. He labelled them "production management," "capacity constrained" and "severe oscillation" periods. The important question, he said, "is not if, but when the next period of [supply] tightness will occur."

The great American public, meanwhile, is taking all this in stride. The *Wall Street Journal* reported in mid-April that the joint opinion poll it takes with NBC News indicates that three-fourths of the people believe the break they are getting in lower prices for gasoline and fuel oil will last less than a year. Nine out of 10 still think it is important to conserve energy and 76% believe the U.S. will have another crisis within 10 years. Of these, 36% emphasized that the probability of a crisis was "very likely." NPN

First Quarter Earnings

Company	1st Qtr. 1986 (millions of dollars)	1st Qtr. 1985 (millions of dollars)	% Chng.
Exxon	$1,710.0	$1,325.0	29.1%
Mobil	440.0	320.5	37.5
Chevron	356.0	354.0	0.6
Texaco	328.0	320.5	2.5
Shell	276.0	296.0	(6.8)
Amoco	331.0	473.0	(30.0)
Tenneco	124.0	(54.0)	—
Atl. Richfield	288.0	352.0	(18.2)
Standard Oil	253.0	343.0	(26.2)
Phillips	96.0	113.0	(15.0)
Sun	146.0	127.0	15.0
Unocal	70.2	180.7	(61.2)
Amer. Hess	(339.3)	37.2	—
Dia. Shamrock	(10.0)	59.1	—
Ashland (*)	39.0	14.0	178.6
Kerr-McGee	22.1	28.4	(22.2)
Pennzoil	42.3	57.4	(26.3)
Murphy	10.9	26.2	(58.4)
Am. Petrofina	(39.7)	2.5	—

(*)Second quarter, fiscal ends 9/30; for comparison, first quarter was $49 million vs. $26 million.

Downstream Earnings

Company	1st Qtr. 1986 (millions of dollars)	1st Qtr. 1985 (millions of dollars)	% Chng.
Exxon			
Domestic	$160.0	$13.0	1,131%
Foreign	447.0	16.0	2,694
Mobil			
Domestic	51.0	(11.0)	—
Foreign	204.0	(3.0)	—
Chevron			
Domestic	37.0	(25.0)	—
Foreign	121.0	78.0	—
Texaco			
Worldwide	301.0	(27.0)	—
Shell			
Domestic	61.0	8.0	663
Amoco			
Worldwide	19.0	2.0	850
Atl. Richfield			
Domestic	89.0	49.0	87
Standard Oil			
Domestic	10.0	52.0	(80.0)
Phillips			
Domestic	98.0	2.0	4,800
Foreign	20.0	7.0	186
Sun			
Domestic	68.0	20.0	240
Foreign	(4)	1	—
Kerr-McGee			
Domestic	(2.4)	(13.7)	—
Amer. Hess			
Domestic	(374.4)	(19.2)	—
Ashland*	59.9	15.9	277

*Second quarter, fiscal ends 9/30.

Unleaded to Reach 70% Of Demand This Summer

The probability that seven out of every 10 gal. of gasoline sold this summer will be unleaded emphasizes how fast and how far the marketing industry has come in the federally mandated transition from the leaded to an unleaded gasoline economy.

American Petroleum Institute noted recently that unleaded sales already were at the 68% level in March. Thus, in little more than a decade, unleaded gasolines have gone from ground zero to absolute dominance of motor fuel marketing. The transition began in 1975.

In peak year 1978, gasoline consumption averaged 7,412,000 b/d with unleaded amounting to 34% or 2,421,000 b/d. Consumption declined to 6,539,000 b/d in 1982 but has been increasing modestly since then. In 1985, consumption averaged 6,815,000 b/d, with almost 65%, or 4,395,000 b/d being unleaded grades.

Leaded premium has all but vanished from the American scene and leaded regular appears to be only a couple of years away from the point when its share of market will be virtually insignificant—probably less than 10%.

Another interesting factor is that under federal regulations there really isn't much difference between the leaded and unleaded gasolines. Federal regulations now specify that lead content of regular fuels cannot exceed 0.1 grams/gal. The same regulations tolerate 0.05 grams/ lead in unleaded fuel. That means the mathematical difference is about 1/20th gram/gal.

Energy Information Administration, in a commentary on gasoline sales in its *Petroleum Supply Monthly*, had this to say:

"Unleaded gasoline sales grew in all regions in 1985.

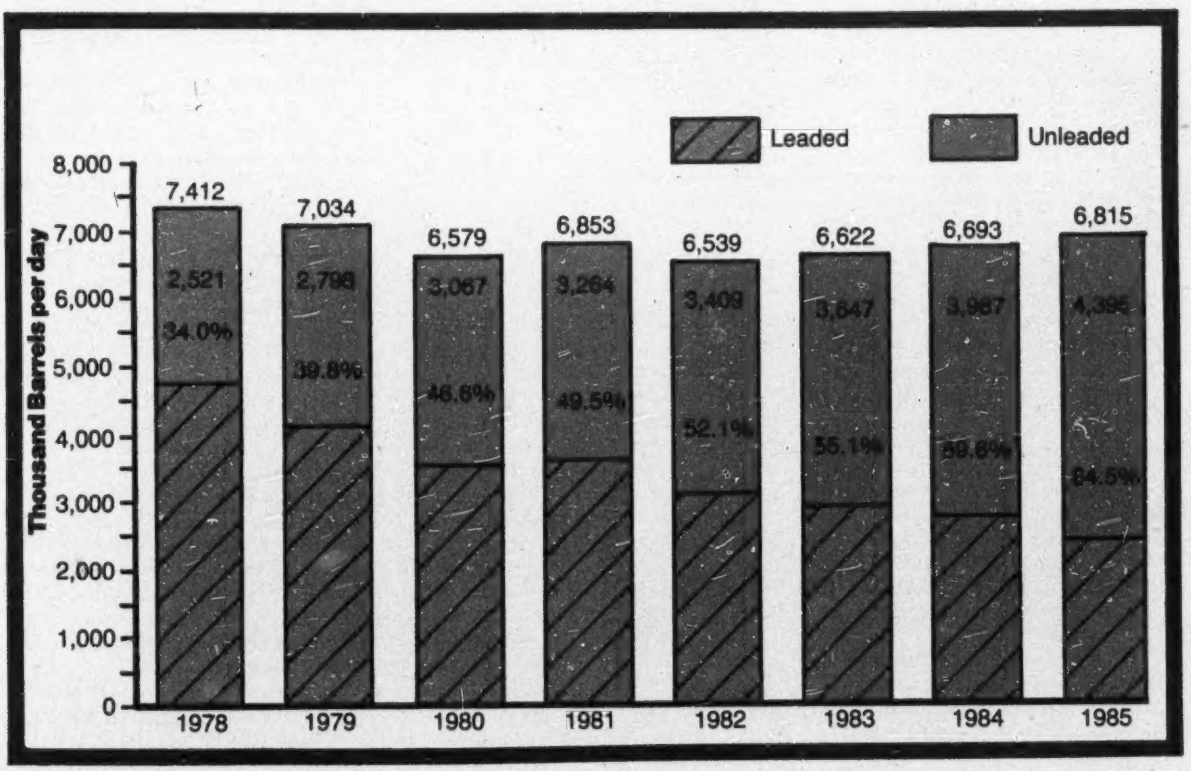
"Unleaded gasoline sales accounted for 72% of all gasoline sales on the West Coast, 71% on the East Coast, 64% on the Gulf Coast, and 60% in the Midwest. The Rocky Mountain area was the only region where unleaded accounted for less than half of the gasoline consumed.

"Gasohol consumption continued to increase in 1985, rising to 409,000 b/d, an increase of 16% from 1984. However, this increase was less than 27% between 1983 and 1984."

EIA also noted that most of the vehicles using leaded gasoline are the pre-1975 models. While these vehicles comprise an estimated 31 million cars and 14 million trucks (28% and 35% of vehicles in operation), scrappage rates increase with the age of the vehicles themselves.

Studies show that 50% of the vehicles for a model year are scrapped at 10.9 years for passenger cars and 12.0 years for light trucks, with 2% of the passenger cars and 24% of the light trucks surviving for 20 years, EIA says. **NPN**

Unleaded vs. Leaded Motor Gasoline, 1978–1985



Source: Energy Information Administration, Petroleum Supply Monthly, February 1986.

C-store Briefs

Two-thirds of Convenience Stores Are Now Selling Gasoline, Report Says

Having started from almost ground zero a decade ago, the growth of convenience stores selling gasoline has been phenomenal.

According to John Roscoe, a West Coast C-store chain operator and author of the annual "Dollars Per Day Survey of the Small Food Industry," nearly two-thirds (65%) of the estimated 58,000 convenience-type stores in the United States now market gasoline.

Roscoe's 1986 Dollars Per Day Survey, which is an analysis of the top nine publicly owned C-store chains to represent the industry as a whole, estimates that all C-type stores, including traditional stores and other food and gasoline combinations, sold 16,808,446,000 gallons in 1984 or 14.3% of the highway gasoline marketed in the U.S. The average store sold 1,227 gallons of gasoline per day.

Roscoe says that C-type stores increased their percentage of the national gasoline market by 1.87% in 1984, and he estimates that over 20% of the gasoline sold in the U.S. in 1985 was sold through C-stores. By contrast, he says, in 1976 only 1% of total U.S. gasoline volume was sold through convenience stores.

As for the nine chains cited in the survey, they sold 3,281,690,023 gallons in 1984, an increase of about 12% over the previous year. These nine accounted for 3.24% of total U.S. gasoline sales in 1984 through their 7,592 stores. Gasoline made up almost one-third (32.6%) of the total sales of the nine chains.

Ranking the nine firms in terms of pretax profits, Roscoe cited Shop & Go, Mango, Fla., as the most profitable for the fifth straight year. Following in descending order were Circle K, Phoenix, Ariz.; National Convenience Stores, Houston; Southland Corp. (7-Eleven), Dallas; Casey's General Stores, Des Moines, Ia.; Sunshine Jr. Stores, Panama City, Fla.; Munford Inc., Atlanta; Dairy Mart Convenience Stores, Enfield, Conn.; and Conna Corp., Louisville, Ky.

Cumberland Farms Inc., a privately-held eastern C-store chain not included in the Dollars Per Day survey, recently took over the mantel as the nation's number one independent gasoline marketer. Cumberland, which acquired most of Chevron's northeast marketing facilities in late-1985, boosted its annual gasoline volume to about the 2.65 billion gal. a year level at the take-over date. Cumberland now has about 3,860 outlets, but many are former Chevron and Gulf gasoline stations, at least temporarily.

Another study of the C-store business by the federal government, although limited to franchised outlets, tends to confirm Roscoe's findings. The government data (see Franchise Projections table below) projects the franchised C-store population will pass the 16,000-unit level by the end of 1986. Although the growth rate of franchised operations was somewhat slower than the year-ago projection (2.4% versus the forecast 4.4%), the government says this year's growth rate should more than double last year's to 5.3%. Even more interesting is the government's prediction that total franchised sales and services will increase by a whopping 13.3% in 1986 to $12,369,139,000.

As convenience store companies extend their penetration into the gasoline market, so, too, are petroleum marketers expanding their involvement in the C-store field. Eleven of the 14 largest integrated oil companies now supply 10,045 C-stores, with 2,109 of those being direct operations [*NPN*—May '86, p49]. These figures are lower than the actual numbers of convenience stores operated by the majors since three companies with extensive networks of C-stores declined to disclose the number of units they own. *NPN*

Government Franchise Projections

	1986	1985	1984	Percent Changes '85-86	Percent Changes 1984-85
Total number of establishments:	16,120	15,314	14,960	5.3%	2.4%
Company-owned	9,204	8,796	8,507	4.6	3.4
Franchisee-owned	6,916	6,518	6,453	6.1	1.0
Total sales of products and services: ($000)	$12,369,139	$10,911,314	$10,292,508	13.3	6.0
Company-owned	7,731,205	6,685,410	6,304,904	15.6	6.0
Franchisee-owned	4,631,934	4,225,904	3,985,604	9.6	6.0

Distribution by Establishments—1984

Size Groups	Franchising Companies Number	Establishments Number	Establishments %	Sales ($000)	Sales %
1001 and Greater	4	11,558	77.3	$ 8,756,806	85.1
501 - 1000	7	2,912	19.5	1,276,145	12.4
151 - 500					
51 - 150	5	359	2.4	192,613	1.9
11 - 50	5	112	0.7	56,834	0.5
0 - 10	3	19	0.1	10,110	0.1
Total	**24**	**14,960**	**100.0**	**10,292,508**	**100.0**

Source: "Franchising in The Economy, 1984-86," U.S. Department of Commerce, February 1986.

Mich. C-stores Form Trade Association

Convenience store owners and operators in Michigan formed an independent, not-for-profit association this spring to represent their industry.

Chris Kindsvatter, executive director of the Convenience Store Assn. of Michigan, says the association will represent the industry at public hearings, lobby the state general assembly on industry-related legislation, and provide educational seminars for C-store operators.

Kindsvatter says the association was formed because C-store owners felt like a "second child" to the state's food and drug industry and petroleum marketers group. Those organizations would not have the expertise in C-stores that CSAM would have, he says, and the National Assn. of C-Stores (NACS) can't focus on state issues.

There is no competition between CSAM and the other organizations, Kindsvatter says. In fact, many of its members are part of other associations. CSAM's first president, Jim Hinton, of Imperial Oil Co., is a member of the Michigan Petroleum Assn.

Kindsvatter estimates Michigan has between 250 and 300 companies operating C-stores. Of those companies, 30 (representing 500 stores) have joined CSAM during its first month of operation. CSAM also has 10 associate members, he says. Among the new members of CSAM are Southland, Stop-N-Go, Quality Dairy and Pri Mar, he says. *NPN*